FISCAL NOTE
HB 20 - SB 37
FIRST EXTRAORDINARY SESSION

April 7, 1999

SUMMARY OF BILL: Imposes the franchise and excise tax on limited liability partnerships, limited liability corporations, sole proprietorships, partnerships, and any other organization or entity engaged in a for-profit business in Tennessee. The commissioner of revenue would be authorized to collect excise and franchise taxes from any business organized for profit regardless of its method of organization, unless such entity has a not-for-profit exemption under the Internal Revenue Code or has a specific exemption under Tennessee law. Bill also redefines "business earnings" under the excise tax laws to provide that the corporate owner of a pass-through entity that participates in the management or control of the pass-through entity, directly or indirectly, by virtue of an affiliated corporation, would be deemed to be engaged in the pass-through entity unitary business activity. If a tiered pass-through entity were involved, the ultimate owner of the tiered pass-through entity would be deemed to be the owner of the pass-through entity engaged in business in Tennessee. Bill further adds a new provision to excise tax law that provides that a corporate owner of a pass-through entity, that either participates in the management or control of the pass-through entity directly or indirectly by virtue of an affiliated corporation or officers, employees, or directors of the corporate owner or affiliated corporation, would be deemed to own its percentage interest of the assets owned or leased by the pass-through entity. If tiered pass-through entities are involved, the ultimate owners would be deemed to be the owner of the pass-through entity engaged in business in Tennessee. Bill stipulates, if affiliated corporations participate in the management or control of the pass-through entity, the pass-through entity unitary business income would be reported on a combined return by all of the affiliated corporations that are owners of such pass-through entity. The return would reflect the affiliated corporations' combined percentage interest of the operations of the pass-through entity unless the commissioner consents to an election by each of the affiliated corporations to the filing of separate returns in Tennessee reflecting such corporation's percentage interest of the pass-through entity unitary business income. Bill defines "pass-through entity" as a partnership, limited liability company, limited liability partnership and any other unincorporated association on which the owner includes the income, gain and loss of the entity in the owner's federal tax computations.

ESTIMATED FISCAL IMPACT:

Increase State Revenues - $450,000,000

Increase State Expenditures - Dept. of Revenue
Exceeds $3,000,000 Recurring
Exceeds $2,000,000 One-Time

Estimate assumes the following:

- Bill contains no earnings exemption levels for any business entities.
- Partnerships will distribute a significant amount of earnings to partners reducing their net earnings for excise tax purposes significantly.
- Sole proprietorships will pay the 6% excise tax on most net earnings.
- Bill eliminates the use of pass through entities as a method to evade franchise and excise taxes.
- An increase in state expenditures in excess of $5,000,000, in the Department of Revenue, resulting from implementation of a new tax structure.

CERTIFICATION:

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.

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James A. Davenport, Executive Director

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